



**MINUTES FROM THE INVESTMENT SUBCOMMITTEE
OF THE CASH MANAGEMENT POLICY BOARD
AUGUST 9, 2017**

A meeting of the Investment Subcommittee (the “Subcommittee”) of the Cash Management Policy Board (the “Board”) was held on August 9, 2017, 10:00 a.m., in the main conference room of the Office of the State Treasurer (“OST”), located at 820 Silver Lake Blvd., Suite 100, Dover, Delaware.

Subcommittee Members Represented or in Attendance:

Mr. John Flynn, Board Chair
Mr. Dave Marvin, Subcommittee Chair
The Honorable Kenneth Simpler, State Treasurer

Subcommittee Members Not Represented or in Attendance:

Mr. Mike Karia, Subcommittee Co-Chair
Mr. Richard Geisenberger, Secretary, Department of Finance

Others in Attendance:

Mr. Art Jenkins, Policy Analyst, Office of the Controller General
Ms. Nohora Gonzalez, Deputy State Treasurer, OST
Mr. Stephen McVay, Cash Manager, OST
Ms. Susan Steward, Policy Advisor, OST
Ms. Kim Miller, Senior Vice President, The Northern Trust Company (“Northern Trust”)
Ms. Nivia Gilkey, 2nd Vice President, Northern Trust
Mr. John Krimmel, Partner, NEPC, LLC, Investment Advisor

CALLED TO ORDER

Mr. Marvin called the meeting to order at 10:02 a.m.

APPROVAL OF MEETING MINUTES

A MOTION was made by Mr. Marvin and seconded by Treasurer Simpler to approve minutes from the Subcommittee meeting on May 3, 2017.

MOTION ADOPTED UNANIMOUSLY

BOARD RESOLUTION 2017-1 APPROVING AND MEMORIALIZING INVESTMENT ARCHITECTURE FOR THE STATE’S CASH ACCOUNTS

Mr. McVay discussed the resolution memorializing the new investment architecture (as approved at the May 2017 meeting) and explained that it permits the Board to make changes without the need for the Board to amend their formal investment guidelines. The resolution will be attached to the investment management “RFP” to provide context for prospective bidders.

Mr. Flynn noted that a resolution providing flexibility is welcome. Mr. Krimmel requested a change to a footnote on the Budget Reserve Account from \$226 million to \$236 million to reflect the balance as of July 27, 2017. Mr. McVay indicated that OST staff already made the change.

A MOTION was made by Mr. Flynn and seconded by Mr. Marvin to recommend to the Board that it approve the resolution.

MOTION ADOPTED UNANIMOUSLY

PORTFOLIO VALUATION METHODS

Mr. McVay discussed the Northern Trust memo distributed prior to the meeting regarding valuation changes. On December 1, 2016, OST transitioned custodian services from The Bank of New York Mellon Corporation (BNYM) to Northern Trust. In May 2017, an investment manager reported to OST discrepancies on the Northern Trust's performance reports. An investigation initiated by OST in June 2017 concluded that Northern Trust had implemented the wrong method of accounting at the time of transition, which caused issues with performance reporting. In July 2017, Northern Trust provided OST with a memo explaining the error and providing recommendations for resolving the reporting issues.

Ms. Gilkey confirmed that the reporting conflicts were the result of an error during onboarding and provided a recommendation to do a full revision from December 2016 to ensure the most appropriate restatement for auditing. Ms. Gilkey indicated that Northern Trust is working to meet its proposed timeline for restatement of all monthly reports and the annual report for fiscal year 2017.

Treasurer Simpler inquired about which restatements had been already provided per the proposed timeline, if the changes made by Northern Trust would impact market values previously reported to the Board and the estimated size of the reporting change. Ms. Gonzalez indicated that all but the month of June 2017 had been received. Mr. McVay indicated that changes in market values were likely to be immaterial and OST could quantify the change before the next meeting.

Mr. Marvin directed OST to thank the managers for their diligence bringing this matter to the state's attention.

INVESTMENT MANAGEMENT RFP DISCUSSION

Ms. Steward provided an update on the investment management RFP process and proposed timeline. She noted that the RFP document was in the process of being finalized and asked members to submit any suggested changes or proposed additions by August 18, 2017.

Ms. Steward identified the evaluation committee members selected to date and indicated that members of the Board were invited to join the committee. Since no member of the Board were available, OST requested a representative from the Department of Finance. The Subcommittee agreed with the approach.

INVESTMENT ACCOUNTS UPDATES

Land and Water Trust Account

Mr. McVay reminded the Subcommittee in 2015 when the Land and Water Trust Accounts were opened, the three investment managers received \$60 million total. All are invested in mutual fund products, and the investment consultant at the time, Credit Suisse, brought to OST's attention that the managers could not guarantee compliance with the five percent cash requirement.

The Board instructed OST to establish a cash account and OST created a separate account for the Land and Water cash account using \$3 million from operating funds. After the review this year, OST determined that the Board's intention at the time was to have the cash account funded from the land and water trust accounts. On July 17, 2017, OST transferred the \$3 million back to the operating account and requested that the portfolio managers raise five percent cash based on year-end balances for fiscal year 2017 to be transferred into the new cash account. Mr. McVay indicated that OST will true up the account each quarter for compliance.

Budget Reserve Account (the "Rainy Day Fund")

At the end of July 2017, OST received notification from the Department of Finance to increase the Rainy Day Fund from \$231 million to \$256 million. Mr. McVay reported that in 2016 the Subcommittee requested OST look into the sensitivity of the Rainy Day Fund portfolio to interest rate shocks. OST, NEPC, and JP Morgan confirmed that a \$5 million cushion would protect against a 100 basis point interest rate increase. Therefore, JP Morgan would hold the Rainy Day Fund balance plus an additional \$5 million dollars in case of an interest rate shock. When the balance increased this July, Mr. McVay requested NEPC review the portfolio again to reaffirm the cushion was sufficient. NEPC confirmed the sufficiency of the portfolio cushion of \$5 million thereby ensuring that in the event of an interest rate shock the fund would not be drawn down below \$237 million.

Outside Investment Accounts

Mr. McVay provided an update on four outside investment accounts held by the Court of Chancery and three local school districts. The accounts were opened using the State's EIN but are not managed with the State's accounting system (FSF). The Court of Chancery account (the largest of the four) is in compliance with the Board's investment guidelines and is being managed by PFM, an approved investment manager. Mr. McVay indicated OST requested that the account holders provide additional information to verify compliance with Board guidelines. The Subcommittee discussed its oversight authority and duties with respect to the outside accounts.

NEW BUSINESS

No new business.

PUBLIC COMMENTS

No members of the public present for comment.

NEXT MEETING

The next meeting is scheduled for November 1, 2017.

ADJOURNMENT

A MOTION was made by Mr. Marvin and seconded by Treasurer Simpler to adjourn the meeting of the Subcommittee at 10:40 a.m.

MOTION ADOPTED UNANIMOUSLY

Respectfully submitted,

David Marvin
Chair for the Investment Subcommittee

Mike Karia
Co-Chair for the Investment Subcommittee